Agenda Date: 8/15/01
Agenda Item: 5B

STATE OF NEW JERSEY

Board of Public Utilities

Two Gateway Center
Newark, NJ 07102

WATER AND WASTEWATER

IN THE MATTER OF THE PETITION	)	ORDER DENYING MOTION
OF MIDDLESEX WATER COMPANY	)	
FOR APPROVAL OF AN INCREASE	)	
IN ITS RATES FOR WATER SERVICE	)	BPU DOCKET NO. WR00060362
AND OTHER TARIFF CHANGES	)	OAL DOCKET NO. PUC 4879-00S

(SERVICE LIST ATTACHED)

BY THE BOARD:

By letter dated June 18, 2001, Middlesex Water Company (Middlesex or Company) filed a motion with respect to a rate base determination made by the Board in the context of its June 6, 2001 Order in this matter (Board Order). The issue of concern to Middlesex relates to the Board's treatment of $3.6 million paid by the Company for the purpose of acquiring the South Amboy water system. Specifically, Middlesex asks the Board to revisit its decision not to include $1.6 million of that amount in the Company's rate base. Middlesex claims that in reaching this decision, the Board relied upon "demonstrably incorrect information" (Letter Motion at 1) and was not "fully apprised of all the facts." (Id.at 2). Middlesex further contends that, based upon this alleged mistaken reliance, the Board chose an inappropriate remedy, exclusion of the $1.6 million amount, as opposed to directing that further hearings on the valuation issue be held. (Id). The motion has been opposed by both Staff and the Division of the Ratepayer Advocate (Advocate).

SUBSTANCE OF JUNE 6, 2001 ORDER RELEVANT TO MOTION

In its June 6, 2001 Order, the Board determined to include, as part of the Company's rate base, $2 million of the $3.6 million paid by the Company to acquire the South Amboy water system. At hearing, the Company had sought inclusion of the total $3.6 million purchase price, referring, in summary fashion, to two independent appraisals it had obtained, which concluded that the South Amboy water system was valued in excess of that purchase price. The appraisals, themselves, however, were not entered into the record of the rate proceeding by the Company, nor did any other party seek to introduce them. While discovery with respect to the appraisals was exchanged among the parties,[1] no testimony was presented or cross examination

[1] Parties to this proceeding included Board Staff, the Advocate, and, as intervenors, the Townships of East Brunswick, Edison and Woodbridge, the Borough of Sayreville, the Marlboro Municipal Utilities Authority and the Old Bridge Municipal Utilities Authority.

conducted, concerning the various assumptions, data or methodology underlying the conclusions reached in those appraisals.

Instead, argument at hearing focused upon the rate treatment to be accorded $1.6 million of the total $3.6 million purchase price. Board Staff opposed inclusion of this $1.6 million, arguing that it represented the Company's forgiveness of a prior loan in that amount to South Amboy. Similarly, the Advocate initially excluded $1.6 million of the $3.6 million purchase price in its calculation of the Company's rate base, but later excised the entire $3.6 million based upon its view that the Company had not actually acquired the system, but only the "right to acquire" it in the future. (This argument was rejected by the Board as set forth in the June 6, 2001 Order).

At the Board's April 25, 2001 public agenda meeting, the Board was informed, by its advising Deputy Attorney General, of the fact that the two independent appraisals, which had been specifically required by a prior Board Order approving the related municipal consent (BPU Docket No. WE98121431), had not been entered into the record of this rate proceeding. The Board was further advised that, since the appraisals had been filed with the Board pursuant to the Board's Order in the prior municipal consent docket, the Board could take official notice of the appraisals, but would have to provide the parties with an opportunity to review the full appraisals and submit written comment.

The full appraisals were subsequently provided to all parties to the proceeding. Comments were received from the Company, the Advocate and Board Staff regarding the appraisals. In its May 3, 2001 comments, the Company relied upon the fact that, although the appraisals had not been introduced in the rate proceeding, there had been summary references to the appraisals at hearing and that discovery had been exchanged among the parties, with no party seeking submission of the full appraisals on the record. (Company Comments dated 5/3/01). The Advocate, in its May 2, 2001 comments, objected vigorously to any consideration of the appraisals, arguing that: (1) the appraisals were not in the record and that the parties had not been supplied with full copies of the appraisals prior to the Board's directive; (2) the appraisals allegedly did not conform to uniform standards; (3) the appraisals were based on a "replacement cost new less depreciation" (RCNLD) methodology, rather than the more traditional "original cost" methodology; (4) numerous assumptions and references contained in the appraisals were allegedly devoid of explanation; and (5) the appraisals were not relevant to the valuation of a "right to acquire" the South Amboy system, which, according to the Advocate, was all that the Company had actually purchased. (Advocate Comments dated 5/2/01). Board Staff noted that the quantification of utility plant for rate base inclusion is generally made through a determination of original cost and that the "RCNLD" methodology, upon which the Company's appraisals were based, does not purport to make an original cost determination. (Board Staff Comments dated 5/3/01). Board Staff went on to state that while the RCNLD methodology's potential is best achieved in arriving at a valuation for purposes of setting an appropriate acquisition adjustment, the Company had not sought an acquisition adjustment. (Id).

In its June 6, 2001 Order, the Board determined that it would not rely upon the appraisals because: (1) there was no record exploring the underlying data and assumptions; and (2) the appraisals were not based upon "original cost," the traditional standard for rate base valuations. Consequently, the Board confined its examination of the valuation issue to the record as it was created by the parties to the proceeding. Based upon that record, the Board determined $2 million to be the appropriate amount for inclusion in rate base. This finding was based on the fact that $2 million represented the Company's preliminary estimate of the system's assets and the Company had failed to sustain its burden of demonstrating any valuation in excess of that

preliminary estimate. The Advocate's own expert witness had included $2 million in his calculation of the Company's rate base, and the entire amount was only excised by the Advocate after it changed its legal theory of the case. Finally, both Board Staff and the presiding Administrative Law Judge (ALJ) had recommended a $2 million valuation, based upon the view that $1.6 million of the purchase price presented forgiveness by the Company of a prior loan to South Amboy.

After review of the Initial Decision and the arguments presented by the Company and all other parties, the Board determined to recognize only $2 million in rate base and to exclude the remaining $1.6 million portion of the $3.6 million purchase price, not because it was forgiven loan,[2] but because the Company failed to support any valuation in excess of $2 million at hearing. It is with respect to this rate base determination that Middlesex seeks relief.

POSITION OF MIDDLESEX

(a) Alleged Errors in the Board's June 6, 2001 Order

Briefly summarized, the alleged misconceptions which Middlesex asserts influenced the Board's decision are: (1) a mistaken belief that the other parties had not been afforded a full opportunity to challenge two independent appraisals of the South Amboy system, which valued that system at $4.2 to $6.3 million; and (2) a mistaken belief that the parties had previously "agreed" to a system valuation of $2 million.

With respect to the first alleged error, Middlesex claims that the parties were afforded a full opportunity to address the appraisals at hearing. To demonstrate this, Middlesex relies upon the fact that: (1) the Company "summarized" the results of the appraisals and responded to discovery requests regarding the appraisals (Letter Motion at 6); and (2) a Company witness was asked questions on cross-examination pertaining to the $3.6 million valuation as compared to the higher appraised values. (Id. at 7).

Middlesex further argues that "[a]ll of the parties … were free to request copies of the full appraisals, but elected not to do so." (Id. at 6). As further support for this conclusion, the Company states that "the Staff and the Ratepayer Advocate … had been aware of the full appraisals for more than a year and were free to do whatever they liked about them including requesting them, introducing them into evidence, and relying on them for whatever purpose they wished." (Id.) The Company opines that Staff and the Ratepayer Advocate "were fully aware the appraisals supported the Company's valuation" and "elected not to introduce the appraisals because the data would undermine the positions they wished, for their own reasons, to take." (Id.).

Middlesex goes on to assert that "none of the parties believed introduction of the full appraisals was necessary" and that "not one of the parties … challenged the fairness of the purchase price paid for the South Amboy system" or the "appraised value" of the system. (Id. at 5 and 8). Middlesex also states that both Staff and the Advocate challenged only the form in which a portion of the purchase price for the South Amboy system was to be paid (i.e., by offset of a prior $1.6 million loan to South Amboy) and did not attack the valuations set forth in the appraisals. (Id. at 5).

[2] The Board's June 6, 2001 Order recognized that the assumption of an acquired company's existing debt is a common practice. (Board Order at 14).

Finally, Middlesex argues that the Board's acknowledgement of the benefits to be derived from the South Amboy system is inconsistent with the refusal to permit the entire $3.6 million purchase price to be included in the Company's rate base. (Id.) Similarly inconsistent, according to Middlesex, is the Board's determination to reject two independent appraisals which it had ordered the Company to obtain, in favor of an earlier preliminary estimate by the Company. (Id. at 8).

With respect to the second alleged misconception on the part of the Board (an alleged belief that the parties had agreed to a $2 million valuation), Middlesex states that "the parties have never been in accord on the value of the system." (Id. at 8). Middlesex acknowledges that it presented a preliminary estimate of $2.3 million related to the South Amboy acquisition in a prior municipal consent proceeding before the Board, but points out that the Board stated, in its order approving the municipal consent, that all ratemaking issues would be determined in a rate case and that two independent appraisals were required to support any valuation of the South Amboy system. (Id. at 4). Subsequently, the appraisals were obtained by the Company, demonstrating higher valuations.

In concluding its argument to the Board, Middlesex claims that it has been "treated unfairly in many respects in this proceeding," and that "on some issues, fairness has been notably absent or in short supply." (Id. at 9). To support this claim, Middlesex cites the Board's denial of recovery of monies associated with the Company's incentive compensation program. The Company indicated that it will "[n]onetheless … abide by the Board's decision [on the incentive compensation issue] and hope that the Board's apparent policy will be reconsidered in the future." (Id.). As further evidence of unfair treatment, Middlesex points to what it views as undue delay in the issuance of the final written order in this matter. Middlesex objects to the time consumed by the Board's decision to take official notice of the appraisals and to the time taken in preparation of the final written order in this matter following the Board's oral decision at its May 8, 2001 agenda meeting. Middlesex contends that these "delays" have worked significant financial harm on the Company. Middlesex asks that the Board consider "these additional facts when it rules on [the] Motion for Phase Two Relief." (Id. at 9).

(b) Relief Sought by Middlesex

Middlesex believes there is a sufficient basis in the existing record upon which the Board could correct these alleged errors and reconsider the South Amboy valuation issue without further proceedings. However, it notes alternative remedies. (Id. at 2). These include a Phase II review on the limited issue of the rate base value of the South Amboy system, which it believes could be conducted expeditiously, or reservation of the valuation issue for further consideration in the Company's next filed base rate case. (Id. at 8). The Company states its belief, however, that awaiting the next rate case would result "in delay and additional financial inequity." (Id. at 2).

POSITION OF RATEPAYER ADVOCATE

In a letter dated July 9, 2001, the Advocate argues that the Company's motion is procedurally defective in that neither Board nor Court rules provide for a "motion requesting Phase II relief." (Advocate Reply Letter at 3). The Advocate notes that Board and Court rules provide only for motions seeking rehearing, reargument or reconsideration. The Advocate further contends that "under the guise of Phase II relief," Middlesex "is seeking to provide the Board with information which was available to the Company at the time of the initial filing and which the Company failed to provide." (Id.).

With reference to the Company's contention that the Board was not fully apprised of all the facts regarding the South Amboy acquisition, the Advocate states that, if such is the case, "it is only because the Company failed in its obligation to provide those facts within the context of its rate case." (Id.). Further, the Advocate takes issues with statements by Middlesex placing "blame" upon the Advocate and Staff for failure to request the full appraisals and the Company's inferences that such failure was because the parties knew that the data contained therein would "undermine" their respective positions. (Id. at 3). The Advocate reiterates its position, as previously expressed in briefs and exceptions, that the entire $3.6 million should be excluded from the Company's rate base. The Advocate acknowledges that, as noted by the Board, its witness had initially allowed $2 million to be included in the calculation of the Company's rate base. However, the Advocate explains that it subsequently changed its position and called for the entire amount to be excluded, once the Advocate determined that the Company would not be acquiring actual title to the system, but only what the Advocate terms a "future conditional right to purchase the system." (Id).

In conclusion, the Advocate urges the Board to deny the relief sought by the Company. The Advocate requests, however, that if the motion is granted, it be permitted to provide further testimony on the valuation issue.

POSITION OF BOARD STAFF

In a letter reply dated July 6, 2001, Board Staff argues that, even assuming arguendo the existence of the errors alleged by the Company, such errors do not rise to the level of "harmful error" which would require setting aside or revisiting the matter. Nor, according to Staff, do any of the alleged factual errors detract from the fact that sufficient and substantial credible evidence is present in the record which, "considering the proof as a whole, supports the Board's ultimate findings and conclusions regarding the South Amboy Franchise acquisition." (Staff Letter at 2).

FINDINGS OF FACT AND CONCLUSIONS OF LAW

With respect to the procedural objections raised by the Advocate as to the form of the motion filed by Middlesex, the Board will consider the motion a motion for reconsideration or rehearing pursuant to N.J.A.C. 14:1-8.6. Although Middlesex has styled its motion as a "Motion for Phase II Relief", its substance is that of a motion for reconsideration or rehearing. In fact, reconsideration, as well as reservation of the valuation issue until the Company's next rate case, are specifically raised by Middlesex in its motion as possible alternatives to a Phase II proceeding.

With respect to the substantive arguments raised by Middlesex in its motion, the Board has reviewed its final written order in this proceeding, dated June 6, 2001, as well as the transcripts of both the April 25 and May 8, 2001 public agenda meetings, which the Company has attached to its motion. That review reaffirms that the Board was under no misconception as to: (1) the relevant facts surrounding the South Amboy acquisition; (2) the extent to which the appraisals at issue were, or were not, addressed at hearing; or (3) the respective positions of the parties as the system's appropriate valuation.

The Board was fully apprised of the facts involving the South Amboy valuation issue. First, the Board Order acknowledges that the Company had referenced the appraisals on the record, in summary fashion. (Board Order at 11). Also acknowledged in the Board's Order is the fact that all parties knew of the existence of the appraisals, yet did not seek to have them presented on the record. (Board Order at 12). The Board Order further notes the Company's statement that

discovery had, in fact, been exchanged with respect to the appraisals and that no party sought to contest the ultimate conclusion reached. (Id).

In addition, the Board's Order reflects careful consideration of the comments received by the parties, both as to the relevancy of the appraisals to the valuation issue, as well as to the extent to which the appraisals were addressed on the record of the rate proceeding. (Id.). Moreover, the Board, in its June 6, 2001 Order, indicates that, even were it to consider the appraisals, the appraisals themselves were of limited value in that they did not address original cost, the traditional basis for valuation of rate base items. (Id.).

Similarly, a review of the Board's Order reveals no assumption that the parties had reached an "agreement" to value the South Amboy acquisition at $2 million, the figure ultimately determined by the Board for inclusion in the Company's rate base. Instead, by identifying various points in time at which each party had put forth a $2 million valuation, the Board was attempting to discern from the record, what portion of the $3.6 million figure might be viewed as undisputed. Clearly, the Company believed the South Amboy system was worth at least $2 million, as evidenced by its preliminary estimate. Clearly, Staff supported a $2 million valuation for rate base purposes, as evidenced by the position taken by Staff in this proceeding. And, clearly, the Advocate, prior to its concern as to the nature of the right being purchased by the Company, initially included $2 million in its calculation of the Company's rate base. Consequently, once the Advocate's attempt to characterize the right acquired by Middlesex as something less than a rate base item was rejected by the Board, $2 million emerged as the undisputed portion of the $3.6 million purchase price. An insufficient record existed to support any higher valuation. (Id. at 12-13).

A reading of the Board's Order in this matter, therefore, demonstrates that the Board was aware of the facts articulated by Middlesex in its motion, but was unpersuaded by them. The Board's full knowledge of the facts is also reflected in the transcripts of the Board's public agenda meeting deliberations. The transcript of the Board's April 25, 2001 agenda meeting indicates that the Board was apprised of the fact that, although the actual appraisals had not been introduced into the record by the Company, summary type representations as to the content of the appraisals had been made during the course of the rate proceeding. (T4/25/01 at 3). The concern remained, however, that, because the full appraisals had not been introduced, they could not properly be considered as part of the record in this case. Consequently, the Board acted properly in taking official notice of the appraisals as filings made in the earlier municipal consent docket and affording the parties herein time in which to file written comments as to the use of the appraisals in the rate proceeding.

Similarly, the transcript of the May 8, 2001 agenda meeting deliberations reveals that the Board was again informed that there had been comments, representations and discussions concerning the appraisals during the rate proceeding, but that the full appraisals themselves had not been placed, nor examined, on the record. (T5/8/01 at 6, lines 6-11). The Board was also informed that while the Company had not introduced the full appraisals, neither had any party sought to have the appraisals presented. (T5/8/01 at 7, lines 16-21). In addition, the Board knew that the appraisals were on file in the earlier municipal consent docket, but that, beyond the filing of the appraisals, no record was created in that docket as to their content. (Id. at 6, lines 12-16).

Middlesex's allegations are further rebutted by the fact that, by the time of the Board's final deliberations at its May 8, 2001 meeting, Middlesex, the Advocate and Staff had all availed themselves of the opportunity to submit written comments to the Board concerning the appraisals and South Amboy rate base issue. (T5/8/01 at 6, line 24 to 7 line 2). In its written

comments with respect to the appraisals, dated May 3, 2001, Middlesex set forth its view of the relevant facts to be considered by the Board, facts which it now claims the Board did not know.

Finally, as to Middlesex's allegation that the Board's refusal to recognize the entire $3.6 million purchase price in rate base is inconsistent with the Board's recognition that the acquisition of the South Amboy system will benefit ratepayers, the Company is characterizing as interdependent two separate ratemaking determinations. A determination that property is used and useful in the rendering of service to the public is part of the process of deciding whether or not that property should be included in rate base. The valuation of that property, however, is a distinct issue. A finding by the Board that the South Amboy system should be included in the Company's rate base is not a finding that it should be included at any price.

Middlesex engages in similarly faulty reasoning when it argues that it is incongruous that the Board would reject appraisals that the Board, itself, required to be performed pursuant to the Board's Order approving the related municipal consent. It was not, and could not have legally been, the intention of the Board to accept at face value whatever appraisals the Company submitted in response to that prior directive. The purpose for requiring the appraisals in the first place, and reserving all ratemaking issues related to the acquisition until a base rate case was that the appraisals would be submitted and tested in a ratemaking proceeding.

Finally, Middlesex's attempt to portray itself as the recipient of unfair treatment and undue delay on the part of the Board is without merit. The time taken by the Board to afford the parties an opportunity to see the full appraisals and respond thereto, was occasioned by the Company's failure to introduce the full appraisals as evidence at hearing. The burden to do so was on the Company, and it should not now be permitted to shift the burden to other parties to this proceeding, nor fault the Board in its efforts to remedy the Company's error and provide the parties with an opportunity to address the full appraisals in the context of this rate proceeding.

As for the time period from the Board's oral decision at its May 8, 2001 agenda meeting, to issuance of the final written order on June 6, 2001, that span of time cannot be viewed as unduly protracted, given the complexity of the issues involved, and the need to ensure that the written order would set forth all necessary findings of fact and conclusions as required by law.

Based upon the foregoing, the Board FINDS that Middlesex has presented no new evidence or legal arguments, which were not available for presentation at the time of hearings in this matter. In essence, the Company's Motion for Phase II relief is an attempt to correct an error on its part (i.e., its own failure to present sufficient evidence to support its valuation of the South Amboy system).

There exists no due process right to a second hearing, either in judicial or administrative settings. See N.J. Bell Tel. Co. v. Bd. Pub. Utility Com'rs, 12 N.J. 568, 580 (1953). Moreover, where a utility's arguments in support of a rehearing reflect merely "disagreement with the Board's treatment of the evidence generally," Courts have upheld the Board's denial of rehearing as a proper exercise of its discretion. (Id. at 581). Here, Middlesex disagrees with the Board's analysis of the evidence presented by the Company at the rate proceedings. Such disagreement is an insufficient basis for demanding reconsideration or rehearing.

The Board, therefore, DENIES the Motion. The Board REAFFIRMS its determination as to the rate base treatment accorded the Company's acquisition of the South Amboy water system as properly reflecting the record created by the parties in this case. In order to ensure that an adequate record will exist in the future, should the Company seek to raise the issue again, the Board HEREY ORDERS the Company to separately maintain books and records regarding the

costs, expenses, revenues and capital improvements associated with the addition of South Amboy to its franchise until such time as the Company files its next rate case. The Company is further ORDERED to annually submit a list of all new construction, its location, and the cost thereof, as well as any mains, pipes, appurtenances and improvements (including mains repaired by Middlesex or its affiliates during the prior year and anticipated for the current year) relating to South Amboy. This information shall be due on the date Middlesex files its annual report with the Board. The filing requirement shall remain in effect until such time as the Company files its next rate case.

DATED: **08/15/01**

BOARD OF PUBLIC UTILITIES
BY:

(SIGNED)

CONNIE O. HUGHES
ACTING PRESIDENT

(SIGNED)

CAROL J. MURPHY
COMMISSIONER

(SIGNED)

FREDERICK F. BUTLER
COMMISSIONER

ATTEST:

(SIGNED)

FRANCES L. SMITH
BOARD SECRETARY

IN THE MATTER OF THE PETITION OF MIDDLESEX WATER COMPANY
FOR APPROVAL OF AN INCREASE IN RATES FOR WATER SERVICE
AND OTHER TARIFF MODIFICATIONS
DOCKET NO WR00060362

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IN THE MATTER OF THE PETITION OF MIDDLESEX WATER COMPANY
FOR APPROVAL OF AN INCREASE IN RATES FOR WATER SERVICE
AND OTHER TARIFF MODIFICATIONS
DOCKET NO WR00060362

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